

Section II

Financial Statement Findings

Department of Corrections

Introduction

The Department of Corrections manages the State's adult correctional facilities and the adult parole system. The Department also operates the Division of Correctional Industries, which manages various enterprise activities. Those activities include a furniture manufacturing facility, various farming and ranching facilities, Colorado state forms production and distribution facilities, an automotive service station, the State's license plate manufacturing facility, and management of the State's surplus property received from the federal government and other state agencies. The Department also operates the Prison Canteen, which sells various sundries to inmates at the various correctional facilities.

The Department expended approximately \$264 million for Department operations and approximately \$31.5 million for its Correctional Industries.

Administrative offices for the Department are located in Cañon City and Colorado Springs. Correctional facilities are located throughout the State and include Buena Vista, Cañon City, Denver, Pueblo, Limon, Ordway, Delta, and Rifle.

The following comments were prepared by the public accounting firm of Grant Thornton LLP, who performed audit work at the Department of Corrections.

Report Surplus Property Received From the Federal Government Correctly

The Department completes a General Services Administration (GSA) Report of Surplus Property (Form 3040) each quarter of the fiscal year. This report details the beginning inventory amount of federal surplus property on hand at the Department, from what types of entities the receipts of the property came, to what types of entities the property was donated, whether items were sold or destroyed, and the ending inventory of federal surplus property on hand. The Form 3040 reports receipts, distributions, and inventory at federal original acquisition cost (cost). The Schedule of Expenditures of Federal Awards is completed using this report with receipts, distributions, and deferred revenue reported at 23.3 percent of cost as prescribed by the General Services Administration. In reconciling the physical inventory on hand at June 30, 1997, to the Form 3040 ending inventory for the quarter then ended, we noted a difference of \$269,000 in original acquisition cost. We determined that the Department recorded a disbursement of equipment which had never been included as

a part of the inventory. Because the shipment was not originally recorded in inventory, but was recorded as a distribution on the Form 3040, the ending inventory on the Form 3040 for the quarters ended March 31, 1997, and June 30, 1997, was understated. Without appropriate records of federal surplus property inventory, the risk of misappropriation of assets increases. In order to ensure accurate reporting to the federal government, the Pharmacy should reconcile Form 3040 to the physical inventory each quarter prior to submission of the form.

Recommendation No. 1:

The Department of Corrections should ensure that all federal program reports are completed accurately to account for all transactions affecting those programs.

Department of Corrections Response:

Agree. The Department has implemented procedures to correct this problem. The supervisor of Surplus Property is ensuring that the original acquisition cost (OAC) on the perpetual inventory system is in agreement with the OAC on GSA Form 3040 prior to issuing the report to GSA.

Department of Health Care Policy and Financing

Introduction

The Department of Health Care Policy and Financing (DHCPF) was established on July 1, 1994, to administer the State's medical assistance programs. The largest of these is the Medicaid program, which reimburses providers for the cost of medical services they furnish to low-income citizens in Colorado. DHCPF is an active participant in health care reform and provides significant resources and information in developing the health care environment in Colorado. DHCPF's expenditures are funded about equally by federal funds and state general funds. Expenditures totaled approximately \$1.6 billion in Fiscal Year 1997. Approximately 95 percent of these expenditures were for Medicaid-related services.

The public accounting firm of Ernst & Young, LLP, performed the audit work at DHCPF as of and for the fiscal year ended June 30, 1997. During its audit Ernst & Young reviewed and tested DHCPF's internal controls over accounting and administrative functions and federal programs. The audit included examination of account balances and evaluation of DHCPF's compliance with state and federal rules and regulations. The auditors identified two areas in internal controls that need improvement: management of accounts receivable and oversight procedures for potential recoveries of Medicaid overpayments to individuals. The following comments and recommendations were prepared by Ernst & Young, LLP.

Improve Management of Accounts Receivable

The Department uses an accounts receivable account to record all Medicaid-related amounts, such as amounts due from the federal government for expenditures of the Medicaid program, amounts due from health care providers for overpayments on the basis of provider billings, drug rebates due from drug manufacturers, amounts due from intergovernmental agency transactions, and smaller amounts due for items such as Medicaid administration. At fiscal year-end, this accounts receivable balance totaled approximately \$120 million. Of the total, approximately \$101 million was due from the federal government and is based largely upon the amount that DHCPF has paid to Medicaid service providers. The federal government reimburses approximately

53 percent of the State's Medicaid payments. Approximately \$19 million in additional accounts receivable was due from Medicaid providers, drug manufacturers, and Medicaid administration costs.

DHCPF has identified its reconciliation processes for accounts receivable as the primary control to ensure that account balances are accurate and that related revenues are recorded and reported properly. Problems with the reconciliation processes were noted during the audits for Fiscal Years 1995 and 1996. During the Fiscal Year 1997 audit we noted that the Department had made improvements in these processes. However, further improvement is needed in reconciliation procedures used by the Department for two significant components of its accounts receivable: amounts due from Medicaid providers and from drug manufacturers.

For amounts due from both Medicaid providers and drug manufacturers, the Department receives information from systems that are external to the State's financial system. In order to ensure the accuracy of information on the State's system, known as COFRS, the Department must reconcile information from these external sources to COFRS. In general, we found three problems with the Department's reconciliation procedures:

- The reconciliation process is incomplete. The Department focuses its efforts on reconciling monthly activity recorded on the external systems with the monthly activity recorded on COFRS. However, the Department does not ensure that the beginning and ending accounts receivable balances for the external systems are reconciled to COFRS. As a result, the Department may not be identifying all errors and making appropriate adjustments.
- Reconciliations were not always performed in a timely manner. We found that reconciliations were done from two to four months after the end of the monthly reporting periods. Timely reconciliations are needed so that accounts receivable balances are accurate for reporting, billing, and collection purposes.
- The Department relies heavily on manual processes to perform its reconciliations. This makes the reconciliations time-consuming and introduces more opportunity for errors. Some of these manual processes could be automated to improve the efficiency of the reconciliation procedures.

We did not find indications that the Department's accounts receivable contained material errors; however, we believe that timely and complete reconciliations should be prepared and reviewed so that the Department can better identify problems, provide more accurate reporting, and turn delinquent accounts over to collections sooner.

Recommendation No. 2:

The Department of Health Care Policy and Financing should improve its management of accounts receivable by ensuring reconciliations are complete and are performed in a timely manner and by further automating the reconciliation process.

Department of Health Care Policy and Financing Response:

Agree. The Department will improve its management of accounts receivable by doing the following activities, which will be completed by November 1998:

1. Strive to eliminate any manual processes that require duplicate effort.
 2. Reconcile provider accounts on COFRS directly to Blue Cross/ Blue Shield balances.
 3. Identify which receivables currently can be reconciled and ensure that these are completed monthly. The supervisor will review and sign off.
 4. For those receivables where a system problem exists, the Office of Accounting & Purchasing will continue to work with the Office of Information Technology to develop the automation process for these receivables.
 5. For the Drug Rebate receivable, the Office of Accounting & Purchasing will work with the Provider Rate Section to finish this system. This will create an automatic feed to COFRS and track the outstanding Drug Rebate receivables.
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Increase Departmental Oversight for Recoveries of Medicaid Overpayments

The State's counties, through the assistance of the Department of Human Services, determine the eligibility of individuals to receive services paid by the Medicaid program. Eligibility for Medicaid is determined based on various factors, including the individual's income. If a person's income increases, he or she may later be determined ineligible for the Medicaid program. In these cases, the Department of Health Care Policy and Financing's fiscal agent determines whether any Medicaid payments were made for the recipient after eligibility was lost. The fiscal agent issues a report that notifies the counties of these Medicaid overpayments, and the counties are responsible for pursuing possible recoveries of the overpaid amounts from the appropriate individuals.

As of June 30, 1997, the fiscal agent's report identified approximately \$2.6 million in potential Medicaid recoveries. We noted several limitations with the report. For example, the report lists Medicaid overpayments dating back to 1992. However, it does not provide systematic aging information so that counties can easily identify more recent overpayments. This would be helpful information to the counties because these overpayments may be the most useful area in which to concentrate collection efforts. Another limitation with the report is that it appears to include amounts that should be written off. Department staff indicate that in some cases, although the counties determine the overpayments are uncollectible, this information is not always communicated to the fiscal agent so that the accounts can be deleted from the report. Lack of systematic aging information and inclusion of obsolete accounts decrease the usefulness of this report to the counties in their collection efforts.

While some of these potential recoveries may not be collectible because of the lack of resources of the population involved, the Department should improve its oversight in this area to ensure that appropriate and helpful information is provided to the counties to aid collection efforts. Since the State funds approximately 47 percent of Medicaid costs, collection of these potential recoveries can represent income to the State's General Fund.

Improved reporting would also enable DHCPF to more clearly track the potential recoveries that have been identified and recovered, and those that are still pending. This would help the Department to provide feedback to the Department of Human Services and the counties on how they are doing with their collection of Medicaid recoveries and areas for possible improvements. Efforts to collect the outstanding amounts need to begin soon after the overpayments are identified, since the ability to collect the amounts can decrease over time as individuals become harder to locate.

Recommendation No. 3:

The Department of Health Care Policy and Financing should improve its oversight of the collection of Medicaid overpayments by improving the tracking, reporting, and analysis of identified overpayments and using this information to aid county collection efforts.

Department of Health Care Policy and Financing Response:

Agree. The Department accepts the recommendation and will modify its reporting to the counties to include systematic aging information and will work with the counties to update the information on a more current basis. We disagree with the amount identified as a potential Medicaid recovery in the report, because this \$2.6 million is the total dollar amount of requests from various counties for information related to potential recoveries. We will seek to clarify the correct amount of potential recoveries with the fiscal agent and county personnel.

The Department will initiate an improved tracking mechanism to provide feedback through the Department of Human Services (DHS) to the counties to better assist them in their collection, tracking, and reporting efforts. Finally, the Department will work with the DHS to encourage the counties to engage in early and intense collection efforts when amounts are ripe for recovery.

Full implementation of this recommendation will depend on the completion of the Colorado Benefits Management System (CBMS). Currently, the scheduled implementation date for the CBMS system is August 2000.

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Department of Higher Education

Introduction

The Department of Higher Education was established under Section 21-1-114, C.R.S., and includes all public higher education institutions in the State. It also includes the Auraria Higher Education Center, the Colorado Advanced Technology Institute, Colorado Commission on Higher Education, the Colorado Council on the Arts, the Colorado Student Loan Division, the Colorado Historical Society, and the Division of Private Occupational Schools.

The State has 24 public institutions of higher education that are governed by six different boards. The governing boards and the schools they oversee are:

- **Board of Regents of the University of Colorado**

University of Colorado at Boulder
University of Colorado at Colorado Springs
University of Colorado at Denver
Health Sciences Center

- **State Board of Agriculture**

Colorado State University
Fort Lewis College
University of Southern Colorado

- **Trustees of the State Colleges of Colorado**

Adams State College
Mesa State College
Metropolitan State College of Denver
Western State College

- **State Board for Community Colleges and Occupational Education (SBCCOE)**

11 Community Colleges

- **Trustees of the University of Northern Colorado**

University of Northern Colorado

- **Trustees of the Colorado School of Mines**

Colorado School of Mines

The audit recommendations to higher education agencies and institutions follow.

State Board of Agriculture

The State Board of Agriculture has control and supervision of three distinct institutions: Colorado State University -- a land-grant university; Fort Lewis College -- a liberal arts college; and the University of Southern Colorado -- a regional university with a polytechnic emphasis. The Board is also responsible for the Colorado State University Agricultural Experiment Station, the Cooperative Extension Service, and the Colorado State Forest Service.

The Board administers the State Board of Agriculture Fund located at the State Treasury. The Board is authorized to fix tuition, pay expenses, and hire officials. The chief academic and administrative officers are the Chancellor of the Colorado State University System and the President of each institution.

Colorado State University System

Colorado State University, Fort Lewis College, and the University of Southern Colorado have been consolidated as a single financial reporting entity -- the Colorado State University System (CSUS).

Colorado State University

The following comments were prepared by the public accounting firm Grant Thornton LLP, who performed audit work at Colorado State University.

Sponsored Programs

The University receives more than \$91,000,000 in federal funds in the form of research and nonresearch grants. These grants are administered through the University's Office of Sponsored Programs. Expenditures of these funds are subject to various controls including authorizations at both the department level and at the Office of Sponsored

Program level. Additionally, the federal government has established specific compliance requirements which apply to all federally funded programs including, but not limited to, allowable costs and activities and monitoring of funds flowing through the University to subrecipients.

Approval of Electronic Journal Entries

The University has developed a Sponsored Programs Manual which outlines policies and procedures related to administration of federally funded programs. A requirement of the manual is that all charges to the sponsored programs exceeding \$1,000 must be approved by Sponsored Program personnel to determine the cost charged to the program is appropriate and allowable. Within the University each Department may approve and execute direct charges to programs through electronic journal entries. Accordingly, charges for federal programs may not be “routed” through the Office of Sponsored Programs for the required approval before the expenditure is made. However, the Office of Sponsored Programs has the option of printing reports for review detailing direct charges to the programs.

This recommendation could potentially affect every federal award with Colorado State University with the exception of the Student Financial Aid Cluster and encompasses the following federal and pass-through entities: The Departments of Agriculture, Commerce, Defense, Education, Energy, Health and Human Services, Interior, Labor, State, Transportation, Treasury; the National Aeronautics and Space Administration; the National Endowment for the Humanities; the National Science Foundation; the Small Business Administration; the Environmental Protection Agency; the Nuclear Regulatory Commission; the United States Information Agency; the Corporation for National and Community Service; Arizona State University; Arkansas State University; Aurogen, Inc.; Battelle, Research Park Triangle; Bechtel Hanford, Inc.; Black Hills Special Services Cooperative of South Dakota; Boulder Innovative Technologies, Inc.; California Institute of Technology, Jet Propulsion Lab; Case Western Reserve University; Centro Internacional De Agricultura Tropical; Consortium for International Development; Colorado River Indian Tribes; Dames & Moore; Denver Public Schools; Duke University; East Tennessee State University; Engineering Incorporated; Environmental Science and Research Foundation; Hagler Bailly Consulting, Inc.; Harvard University; John Hopkins University; Kansas State University; Lockheed Corporation; Lockheed Idaho Technologies Company; Lockheed Martin Energy Systems, Inc.; Marshfield Medical Research Foundation; Martin Marietta Corporation; Michigan State University; Midwest Research Institute; Montana State University; National Jewish Center; Neurex Corporation; New Mexico State University; North Dakota State University; Oak Ridge Associated Universities; Oregon Health Sciences University; Orincon; Pennsylvania State University; Partnership for Environmental Technologies; Purdue University; R.M. Towill Corporation; Rutgers, State University

of New Jersey; Sandia Corporation, Sandia National Labs; Solar Enterprises International, LLC; South Dakota School of Mines; Southern Research Institute; Southwest Regional Laboratories; Southwest Research Institute; Stanford University; State of Kansas; State University of New York; Sterling Research; Survey Research Associates, Inc.; Systems Research & Applications; Texas A & M; Texas Research Institute; the Nature Conservancy; Tulane University; U.S. Enrichment Corporation; UCAR-NCAR-COMET Atmospheric Technical Division, National Center for Atmospheric Research, Research Applications Program and SOARS; Universities of California at Lawrence, California at Los Alamos National Labs, California at Santa Barbara, California at Davis, California at Los Angeles, Alaska at Fairbanks, Connecticut, Denver, Georgia, Hawaii, Iowa, Maryland, Massachusetts at Lowell, Miami, Minnesota, Missouri, Nebraska, Nevada, New Hampshire, Nottingham of England, Puerto Rico, Southern California, Texas at Austin, Vermont, Washington, Wisconsin, Wyoming; University City Science Center; Utah State University; Virginia Polytechnic Institute; Washington State University; Washington University at Missouri; Westat, Inc; and Yale University.

Recommendation No. 4:

Colorado State University should implement a procedure for preapproval of electronic journal entry charges to federal programs that exceed the \$1,000 threshold. All such charges should be reviewed and approved by the Office of Sponsored Programs.

Colorado State University Response:

Agree. The electronic journal entry process will become a part of the new Campus Information System, which includes an electronic approval process. All entries that exceed the \$1,000 threshold will require approval prior to being processed. The current electronic journal entry process provides for an after-the-fact review and approval process. Entries not approved via this process are reversed.

State Board for Community Colleges and Occupational Education

The State Board for Community Colleges and Occupational Education was established by “The Community Colleges and Occupational Education Act of 1967,” Title 23, Article 60 of the Colorado Revised Statutes. The Board functions as a separate entity and, as such, may hold money, land, or other property for any educational institution under its jurisdiction. The statute assigns responsibility and authority to the Board for three major functions:

- Govern the State’s system of community and technical colleges.
- Administer the occupational education programs of the State at both secondary and postsecondary levels.
- Administer the State’s program of grants to local district colleges and area vocational schools.

The following comments and recommendations were prepared by the public accounting firm of Arthur Andersen, LLP, who performed audit work at the Colorado Community Colleges and Occupational Education System.

Community Colleges and Occupational Education System

The eleven colleges in the Colorado Community Colleges and Occupational System (CCCOES) include Arapahoe, Aurora, Denver, Front Range, Lamar, Morgan, Otero, Pikes Peak, Pueblo, Red Rocks, and Trinidad.

Front Range Community College

Reconciliation of Cash Reports to the General Ledger

The Federal Cash Transactions Report (PMS 272) is filed monthly to report the activity of the individual colleges related to federal funds and the amount of federal cash on hand. It was noted during the audit of the year ended June 30, 1996, that the amount reported on the PMS 272 and requested from the U.S. Department of Education was less than the actual amount per the general ledger by \$41,379. Front

Range is attempting to resolve this difference and receive reimbursement for this amount through correspondence with the U.S. Department of Education.

Recommendation No. 5:

Front Range should continue to investigate and resolve any noted differences in a timely manner.

Front Range Community College Response:

Agree. During the year ended June 30, 1996, Front Range prepared a schedule, by student financial aid recipient, to indicate the differences between the PMS 272 and the general ledger totaling \$41,379. In connection with the June 30, 1996, audit, this schedule was provided to Ernst & Young who performed certain agreed-upon procedures on the schedule. This schedule was subsequently sent to the U.S. Department of Education as support for the requested reimbursement. Front Range is currently waiting for a response from the U.S. Department of Education.

Department of Human Services

Introduction

The Department of Human Services (DHS) is solely responsible by statute for administering the State's public assistance and welfare programs. Most of these programs are administered through local county or district departments of social services. The Department also manages programs in the areas of youth corrections, mental health, rehabilitation, and developmental disabilities. In terms of appropriations, the Department was the fourth largest of the State's 22 departments in Fiscal Year 1997. In terms of personnel, the Department had 7,570.3 full-time equivalents or FTE (4,361.2 state; 3,209.1 county) and expended approximately \$1.1 billion during the year.

We reviewed and tested the Department's internal accounting and administrative controls, and evaluated compliance with state and federal rules and regulations. While we found the Department had adequate controls overall, we noted continuing concerns in the fiscal management of grant activity related to cash draws made for federal programs. We also noted some issues regarding the use and treatment of federal indirect cost reimbursements and the need for formalized contracting for vendor services in the Division of Disability Determination Services.

Implement a More Comprehensive Fiscal Management System for Federal Programs

The Department administered 83 different federal programs during Fiscal Year 1997. Federal expenditures for these programs totaled about \$569 million. Accounting for these programs is divided between the Program Accounting Section and the Cash Management Section. The Program Accounting Section primarily accounts for expenditures and earned revenues of all federal programs, while the Cash Management Section determines the amount and timing of the federal cash draws. Cash Management staff also execute all draws on federal grant awards.

From the State's point of view, timely request of federal funds is important because this minimizes the time that general funds are used for federal programs in cases

where federal reimbursement is appropriate. State Fiscal Rules require that agencies make draws of federal funds as soon as possible after the use of funds.

The transfer of federal funds from the federal government to states for reimbursement of federal program expenditures is also governed by the federal Cash Management Improvement Act (CMIA). The purpose of CMIA is to ensure that funds are transferred to the State as close as possible to the time the State makes the related expenditures. Under CMIA, if the federal government does not reimburse the State in a timely manner, the federal government could be charged interest, providing the State made its reimbursement request in a timely manner. Conversely, the State could be charged interest for requesting federal funds prior to making program expenditures. The Department had 14 programs that were under CMIA during Fiscal Year 1997. These programs accounted for about \$503 million, or 88 percent of the Department's total federal expenditures.

Department Continues to Work on Cash Management Issues

We identified problems with the Department's cash management process during the Fiscal Year 1995 and 1996 audits. During the Fiscal Year 1997 audit we found some improvements but continued to note problems in this area. Our concerns are related to the need for improved procedures for grant monitoring and the Department's methodology for identifying and executing drawdowns of federal funds to reimburse state general fund expenditures. We did not note problems with federal program expenditures reported on COFRS.

The Department staff indicated that they continued efforts to improve the cash management process during Fiscal Year 1997. Specifically, they expanded the use of a cash management database among the Cash Management and Program Accounting areas. This has allowed the Program Accountants to more easily analyze earned revenues and expected cash draws for federal programs and to resolve differences. Staff were also able to implement an improved system to ensure account coding was consistent between requests for cash draws and the subsequent cash receipts. This is important for accurately tracking the use of various federal grant awards. However, the new system did not prove effective for the draw requests based on disbursements to the counties, which receive the majority of federal funds expended by the Department.

Towards the end of our Fiscal Year 1997 audit the Department reported that it was making significant organizational and procedural changes in Fiscal Year 1998 that it believes will successfully address problems with fiscal oversight of federal programs and the cash management process. We commend the Department for these actions, and we will evaluate the effectiveness of these actions in our Fiscal Year 1998 audit.

Good management of state and federal funds is a critical function for the State from both a legal and business perspective. Because the Department receives a large portion of the total federal funds provided to the State, the Department plays a significant role in the State's cash management. For example, in Fiscal Year 1997 the Department received about 20 percent of the nearly \$2.8 billion in federal funds the State received.

Establish Increased Oversight and Coordination of Grant Activity

The Department needs to strengthen the overall fiscal management system for federal programs in the following areas.

The Department needs to ensure that sufficient systems and controls are in place to monitor the full range of grant activity. Currently Program Accounting staff perform a monthly reconciliation for expenditures, earned revenues, and *expected* cash draws for federal programs. The reconciliation does not include the *actual* cash requested or received for programs; Cash Management staff oversee these activities. Program Accounting staff include actual cash draws only in reconciliations performed at fiscal year-end. In other words, neither Program Accounting nor Cash Management staff routinely perform a reconciliation that integrates all grant activity including expenditures, earned revenue, expected and actual cash draws, accounts receivable, and available balances for federal awards. Given the large number of programs and dollars involved, we believe that an integrated reconciliation should be prepared monthly to help ensure that problems are identified and resolved in a timely manner throughout the fiscal year.

The Department needs to ensure that appropriate information is communicated among Program Accounting and Cash Management staff. We found that, in part because of system weaknesses, Cash Management staff made numerous manual overrides to and transfers within the automated grant accounting system on COFRS during Fiscal Year 1997. One of the major causes of the overrides was the Department's effort to develop a new system to facilitate draws for county expenditures. Due to problems with the new system, the Department erroneously overdrew five federal programs during the year. This resulted in credit balances in some of the Department's accounts receivable for federal programs. As a result, Cash Management staff transferred credit balances for these programs from the receivable account to a payable account. The transferred balances ranged in total from \$22 million to \$38.5 million during January through May 1997 for various CMIA grants.

Program Accounting staff were not notified of these transfers or adjustments on a timely basis, although the changes often affected cash draws. Since Program Accounting staff include expected cash draws in their reconciliation process, it is essential that such information be communicated to them promptly.

The Department needs to improve its methodology for identifying the amount and timing of cash draws and for executing cash draws in accordance with the timing requirements issued by the State Treasurer and required by State Fiscal Rules. For the sample of transactions we tested, we found that most of the time the Department was not in compliance with the cash draw instructions issued by the State Treasurer under CMIA for receiving federal reimbursement. The results of our testing and its implications are discussed below.

Draw Pattern Does Not Meet Requirements

To determine whether the Department's draw pattern was in accordance with the requirements issued by the State Treasurer, we tested 23 cash draws for payments of federal program costs totaling about \$27.7 million. The Department made 15 of these payments through the issuance of warrants, while the other 8 were made by electronic fund transfers (EFTs). We found the following:

Warrants:

- 10 out of 15 draws (67 percent) were made early; the draws were made an average of 1.8 business days early.
- 5 out of 15 draws (33 percent) were made on time.

Therefore, for the sample tested for warrants the Department was not in compliance with the State Treasurer's draw requirements in 67 percent of the cases. While this indicates the need for further efforts, this is an improvement over Fiscal Year 1996, when we found in the draws tested for warrants that the Department was out of compliance 78 percent of the time for the sample tested, and in most cases the draws were late.

EFTs:

We were unable to determine with certainty whether or not the Department was meeting the State Treasurer's draw requirements for EFTs, because the Department was unable to provide sufficient evidence to link sample EFTs tested to the specific cash receipts. Under CMIA, state agencies are required to maintain this information to ensure compliance with timing requirements. On the basis of the best information available to us, we found the following for the sample of EFTs tested:

- 3 out of 8 draws (38 percent) were made early.
- 4 out of 8 draws (50 percent) were made late; the draws were made an average of 6.5 business days late.
- 1 out of 8 draws (12 percent) was made on time.

Therefore, for the sample tested for EFTs the Department was not in compliance with the State Treasurer's draw requirements in 88 percent of the cases. In the case of the three draws that were early, one of the draw requests was made one day early, and in the other two cases, we were unable to determine how early the funds were drawn. This is because the Department had drawn federal funds in excess of its expenditures in a prior period.

Implications of Cash Draw Testing Results

Under the federal Cash Management Improvement Act, drawing federal funds early is a concern because this means the State is requesting federal funds prior to making the related disbursement. This is prohibited under CMIA and could result in federal interest charges to the State, depending on the State's overall pattern of drawing federal funds for these grants. From the federal point of view, late draw requests are not a particular concern.

From the State's point of view, however, late draw requests are a concern because it means that the State does not receive reimbursement as soon as it could for costs that are fronted for federal programs using general funds. This means the State loses the opportunity to earn additional interest on those funds. We calculated the opportunity cost, or the potential interest lost to the State due to the Department's late draws for EFT payments to the counties. These payments to the counties constitute roughly 75 percent of the \$569 million in federal funds expended by the Department. In our testing of EFTs, half of the draws were made late, on an average of 6.5 business days. Although our sample was not statistically based, if the Department regularly drew federal funds 6.5 business days late for 50 percent of its EFT transfers to counties, we estimated that this represents a loss of roughly \$190,000 in interest to the State during Fiscal Year 1997.

Good Fiscal Management Can Decrease Certain Risks and Aid the State's Cash Management

A more centralized fiscal management process will help the Department to lessen certain risks to the State. Specifically, a more integrated monthly reconciliation process can decrease the risk of loss or misuse of funds because it will enable the Department to recognize and correct grant-related problems on a more regular basis. For example, such a process could help with a more timely identification of posting errors among grant awards. These errors need to be resolved in a prompt manner, since federal grant awards must be used within specific time frames.

In terms of cash management, good business practices require that an entity use its cash efficiently. For the State, one way to accomplish this is to ensure that cash draws for federal reimbursement are made as soon as appropriate after general funds are used for federal program expenditures.

Recommendation No. 6:

The Department of Human Services should develop and implement a more comprehensive fiscal management system for federal programs. This should include, but not be limited to:

- a. Designating a central point of responsibility and accountability for the activities performed by the Program Accounting Section and the Cash Management Section that oversees and coordinates all aspects of fiscal management of federal programs including expenditures, earned revenues, cash draws, cash receipts, related account balances, and federal awards.
- b. Placing in operation an improved methodology for the cash management process that identifies the amount and timing of cash draws and tracks information linking specific disbursements to cash draws and cash receipts.
- c. Implementing an integrated monthly reconciliation process that includes all program-related financial activity such as expenditures, earned revenues, expected and actual cash draws, and cash receipts.
- d. Establishing better controls over fiscal management to ensure that the Department meets state and federal laws and regulations.

Department of Human Services Response:

- a. Agree. Starting in January 1997, the Department began working toward a central point of responsibility for cash management activities. To date, the items the Department has done to meet this goal are:
 - 1. Conversion of the duties of an existing position enabled us to transfer the monitoring of cash management to the Program Accounting Section.
 - 2. The position designated for cash management was filled in May of 1997.
 - 3. The training of the person hired in May of 1997 to assume the duties of monitoring cash management was completed in December of 1997.
 - 4. Establish a database for queries by program accountants for the purpose of establishing information to reconcile cash management draws.
 - 5. Upgrade of the accounting computers for the purpose of establishing the capacity for program accountants to make queries into the database.

The foregoing has resulted in a change in the section within the accounting division that is assigned the responsibility for cash management.

- b. Agree. The response to “1.a.” puts into place a cash management process with the purpose of identifying an amount and timing for cash draws. The new process lists the specific disbursements which are summed daily to an aggregate amount and serves as a basis for the cash draw.
 - c. Agree. We have in place a monthly reconciliation process for federal program-related expenditures and earned revenues. We are developing a reconciliation process for cash draws.
 - d. Agree. We believe the above changes will establish better controls over cash management.
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Purchase of Services Needs Improvement Within Disability Determination Services

The Division of Disability Determination Services (DDS) within the Department assists the U.S. Social Security Administration (SSA) in determining if individuals are eligible for federal disability insurance. In order to make these determinations, the Division pays vendors (physicians) to perform examinations of disability insurance claimants. Examinations are needed when the medical evidence provided by the claimant's physician is inadequate. Examinations are 100 percent federally funded under the Social Security - Disability Insurance program (CFDA #96.001). The Department received nearly \$14 million under this program in Fiscal Year 1997.

The Division's current method for acquiring personal services for claimants' examinations is to use an Authorization for Diagnostic Services form. Staff consider this form to be a one-time contract between the State and the vendor for each claimant. Although this form does indicate the claimant's name, type of examination to be performed, and the price to be paid for the service, the form does not meet requirements for state-approved contracts.

The Division has established a fee schedule that it follows when paying physicians for medical procedures related to consultative exams. This schedule outlines different rates to be paid for each type of procedure depending on time involved, complexity of the procedure, and geographic area.

In Fiscal Year 1997 the Division had 351 vendors listed on its computer database. The database provides a vendor list for each exam based on historical performance data, type of exam required, proximity to the patient, and appointment availability. Disability examiners then employ personal judgment in selecting a vendor based on their prior knowledge of or familiarity with the vendor.

Our audit identified two main concerns with the Division's procedures for purchasing personal services. First, the Division does not use a competitive bidding process and state-approved contracts when obtaining services from vendors receiving significant amounts of state business. Second, the Division does not regularly review or evaluate its fees.

Ten Vendors Receiving Over \$25,000 Each Did Not Have Contracts

We found that the Division is not using state-approved contracts or a competitive bidding process for purchasing services from vendors. State Fiscal Rules and federal procurement procedures require an agency to negotiate and process state contracts when acquiring personal services over \$25,000, and state statutes require state contracts to be awarded through a competitive bidding process, except for specific circumstances. During Fiscal Year 1997 the Division paid over \$2.2 million to 351 consultative exam vendors. Of these 351 vendors, 10 were paid over \$25,000. The Division had not established state-approved contracts with any of these ten vendors. DDS paid over \$1.7 million, or 76 percent of its total expenditures for consultative examinations, to these ten vendors.

Among these ten vendors, we noted one physician who received about \$111,000 in Fiscal Year 1997 for consultative exams. In another case, a medical conglomerate employing 25 doctors received over \$1 million, or 45 percent of the total amount expended by the Division for exams. It might be expected that average fees paid to the conglomerate would be lower because of greater volume. However, the average cost per medical procedure paid to the conglomerate was about \$6 greater, or approximately 6 percent more, than the average cost per procedure paid to the other nine vendors receiving \$25,000 or more in Fiscal Year 1997.

The Division Is Not Adequately Monitoring Its Fees

Although the Division has a fee schedule, the schedule was established nine years ago and may not appropriately reflect current rates. Also, staff reported that they sometimes make informal case-by-case adjustments to the fees based on limited availability of physicians in some geographic areas and the specialization that a procedure may require. Staff also reported that individual negotiations with physicians sometimes result in two different physicians in the same area receiving different fees for the same procedure.

In addition, we noted that federal regulations provide that fees paid for medical procedures should not exceed the highest rates paid by federal or other state agencies for the same or similar types of service. However, Division staff indicated that they do not monitor for this requirement when higher fees are paid than those set out in the fee schedule.

Division Should Review and Improve Procedures for Purchasing Personal Services

Under its current process, the Division is not adequately protecting the State's interest. First, the Authorization for Diagnostic Services form lacks essential elements found in state-approved contracts. For example, the form does not contain an indemnity clause which sets the vendor out as an independent contractor. This clause is important because the State has a third-party liability for the acts of its employees, whereas independent contractors are liable for their own actions. Second, the Division may not be obtaining services in the most cost-efficient manner because it is not using competitive bidding to procure services and monitoring its fee setting and related procedures. Finally, the State is at risk for lawsuits from vendors because the Division is not purchasing services in accordance with state statutes and, therefore, it is not ensuring fair and equitable treatment to all vendors. As mentioned above, one vendor received over 45 percent of the exam expenditures and was paid an average of \$6 more per medical procedure for Fiscal Year 1997. This may create a perception that the Division is not providing other vendors with a fair opportunity to obtain state business or paying vendors in an equitable manner.

Division staff report that they have not used state-approved contracts, since they do not know in advance which vendors they will use. However, we found that the Division has sufficient historical data to anticipate which vendors are likely to receive \$25,000 or more.

By using state-approved contracts, competitive bidding, and monitoring fees, the Division will be able to obtain services in the most cost-efficient manner while complying with state and federal requirements. In addition, the Division will gain assurance that vendors have a fair opportunity to obtain state business.

Recommendation No. 7:

The Department of Human Services Division of Disability Determination Services should review its procedures for purchasing personal services. This review should include:

- a. Competitively bidding in areas where there are available providers to establish a qualified contractors list.
- b. Reviewing the current fee schedule for geographic areas where bids are not solicited, and standardizing procedures for rate adjustments.

- c. Ensuring compliance with federal and state regulations.

Department of Human Services Response:

- a. Agree. The Department will competitively bid in areas where there are available providers.
- b. Agree. The Department will review the current fee schedule and standardize procedures for rate adjustments.
- c. Agree. The Department will seek approval of any new procedures where applicable, from federal authorities and from the State Controller.

State and Veterans Nursing Homes

The Department of Human Services (DHS) is statutorily responsible for the operations of the State's five nursing homes. The homes are located in Trinidad, Florence, Homelake, Rifle, and Walsenburg. All five homes are Medicaid certified and are visited regularly and licensed by the Department of Public Health and Environment. All of the homes except Trinidad are certified by the U.S. Department of Veterans Affairs (VA) to receive federal funds in support of the care of veterans. These four facilities (Florence, Homelake, Rifle, and Walsenburg) are subject to VA regulations and are surveyed annually by VA.

The Department directly supervises and is responsible for the operations of the Trinidad, Florence, Homelake, and Rifle homes. For the Walsenburg facility, the Department has contracted with the Huerfano County Hospital District (District) to operate the home. Under the contract the District has assumed responsibility for financing operating deficits of the home and has a claim on residual assets, if any, after contractual obligations are met.

The following comment and recommendation is from our September 1997 compliance audit of Department of Human Services State and Veterans Nursing Homes.

Report Information on Colorado State Veterans Nursing Home at Walsenburg

The Department of Human Services is required under statutes to submit to the General Assembly an annual report detailing the financial status of each of the State's five nursing homes. However, the Department's report to the General Assembly does not provide accurate financial information on the Colorado State Veterans Nursing Home at Walsenburg. The Department's reporting on the Walsenburg home is inaccurate because the Department uses the State's accounting system, COFRS, as the basis for its report. However, the Walsenburg home's operations are not included on COFRS; only limited information largely reflecting the Huerfano County Hospital District's reimbursement to the State for certain personnel and related services appears on COFRS. As a result of this deficiency on COFRS, the Walsenburg home's operations are also not reported in the State's annual financial statements.

We believe that reporting the Walsenburg home's complete financial activity on COFRS and on the State's financial statements is the correct treatment under accounting standards because the Walsenburg home is a state entity created under state law. Existing statutes make no provision for the home to be recognized as a legally separate entity from the State. The State and the District have mutually agreed that the State owns the home, including the building and the land on which it is located. The federal government requires that the home be state-owned as a condition of receiving federal funds and considers the State to have ownership of the home. In other words, the treatment of the Walsenburg home for reporting purposes should be the same as the other state and veterans nursing homes.

Including the home's activity on COFRS would also address another problem. To date there has not been an audit done on the Walsenburg home in accordance with the federal Single Audit Act. The requirement for this type of audit is stated as part of the postassistance requirements for the federal Veterans State Nursing Home Care Program (CFDA #64.015) under federal regulations for VA-certified facilities, in cases where federal financial assistance exceeds a certain dollar threshold. Since the Walsenburg home's receipts of federal VA funds exceeded the specified threshold for 1995 and 1996, the home should have had this type of audit for those periods. The District's auditors did not perform these procedures during their audits for 1995 or 1996, because they were unaware of these requirements for this particular program. Under federal regulations, noncompliance with requirements can result in loss of funding or other sanctions. If the home were included on the State's financial statements, its activity would become part of the population of transactions covered by the Statewide Single Audit performed by the State Auditor's Office.

Recommendation No. 8:

The Department of Human Services should improve its financial reporting on state and veterans nursing homes by:

- a. Recording on COFRS the financial activity from operations of the Colorado State Veterans Nursing Home at Walsenburg.
- b. Including a full accounting of the Colorado State Veterans Nursing Home at Walsenburg's operations in reports to the General Assembly.
- c. Ensuring that any future contractual arrangements for state and veterans nursing homes provide for inclusion of the home's complete financial information on the State's accounting system and the State's annual financial statements.

Department of Human Services Response:

- a. Disagree. The Colorado State Veterans Nursing Home at Walsenburg's contract with the Huerfano County Hospital District specifies that all revenues and expenses of the Colorado State Veterans Nursing Home at Walsenburg are the responsibility of the contractor and not the State. Given this, the Department believes it would be inappropriate to include the financial operations of this nursing home in the State's financial system.
 - b. Agree. The Department of Human Services will include a full accounting of the Colorado State Veterans Nursing Home at Walsenburg's operations in reports to the General Assembly.
 - c. Disagree. This response is contingent upon legislative direction that the Department plans to seek concerning the current nursing home statutes. These efforts will clarify the Department's level of responsibility and oversight role for the Walsenburg home. The Department will also initiate discussions with the Huerfano County Hospital District to amend the current operating agreement. Items to be reviewed will include ensuring that the District is responsible for fulfilling the "single audit" requirements.
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The Division of Vocational Rehabilitation

The Division of Vocational Rehabilitation is organizationally located in the Department of Human Services in two of its major offices: the Office of Health and Rehabilitation and the Office of Direct Services. The Division of Vocational Rehabilitation's largest program is its Rehabilitation Services program which assists eligible persons with disabilities in attaining employment. In Fiscal Year 1996 the Rehabilitation Services Program was allocated about \$21 million in federal funds and \$5.5 million in general funds and cash funds exempt for a total allocation of \$26.5 million. The Rehabilitation Services program was allocated 227.5 FTE in Fiscal Year 1996 and is the largest of the Division's programs.

The following comments and recommendations are from our August 1997 performance audit of the Division of Vocational Rehabilitation.

Ensure Compliance with State and Federal Procurement Rules

In Fiscal Year 1996 the Division of Vocational Rehabilitation spent approximately \$13 million on services provided to consumers. These services are provided under the "Rehabilitation Services -- Vocational Rehabilitation Grants to States" (CFDA #84.126). Services provided range from the provision of a bus pass to complex mental health counseling, college tuition, and even surgery. In Fiscal Year 1996 the Division used nearly 5,000 different vendors, or service providers, to serve almost 20,000 clients. The majority of the Division's rehabilitation services are purchased through the Case Service Authorization system. This system allows counselors to purchase many of the services as they are needed for clients without needing several different levels of approval, as is required with State contracts. In this system, counselors use forms that are similar to state purchase orders to approve services for individual clients.

Methods Used to Purchase Services Could Be Improved

Because the Division uses a decentralized system for purchasing services, the Division does not take advantage of the benefits of competitively bidding its services. Benefits of the competitive bidding process include (1) encouraging competition among various providers, (2) allows the Division to maximize the purchasing value of public

funds, and (3) allows the Division to ensure the fair and equitable treatment of all service providers.

The State Procurement Rules state that “agencies may procure services up to a limit of \$25,000 without the benefit of competition.” We found that the Division is not using the bidding process to purchase these services. For example, the Division spent \$381,000 on psychological evaluations in Fiscal Year 1996. Of this amount, one vendor was paid almost \$140,000, or more than 36 percent of the Division’s total expenditures on this service. In addition, this vendor did not provide these services under any type of contract with the Division of Vocational Rehabilitation. Three other vendors were also paid more than \$25,000 each for performing psychological evaluations in Fiscal Year 1996 without having to submit a bid or comply with the requirements of a State contract. This is an inappropriate business practice that may put the Division and the State at risk of litigation from vendors who believe they may have been excluded from participating in State contract work.

In addition to the State Procurement Code, federal regulations require that when purchasing services with federal grant monies, “a state will follow the same policies and procedures it uses for procurement from its non-federal funds.” Therefore, by not complying with the State Procurement Code, the Division is also not in compliance with the federal requirements. If not corrected, this practice could potentially result in the loss of federal funding. In addition, the federal “Common Rule” sets forth the documentation requirements for the procurement process. The “Common Rule” states that, “grantees and subgrantees will maintain records sufficient to detail the significant history of a procurement. These records will include, but are not limited to the following: rationale for the method of procurement, selection of contract type, contractor selection or rejection, and the basis for the contract price.”

We feel that the Division could competitively bid some of the Division’s services and contract with multiple providers to provide those services at specified costs. This will still allow for each consumer to choose from among several service providers and therefore, does not limit consumer choice. In addition, this will allow the Division to take advantage of lower prices and more efficient purchasing of services through the competitive bidding process.

Recommendation No. 9:

The Division of Vocational Rehabilitation should:

- a) Examine the types of services it purchases and develop a process for competitively bidding those services that it is required to under the provisions of the State Procurement Code, State Fiscal Rules, and the Federal Common Rule.
- b) Work with the Division of Purchasing to ensure that its new procedures comply in all respects with the purchasing requirements and that they are using the most efficient methods possible to procure services.

Division of Vocational Rehabilitation Response:

Agree. The Division agrees that it needs a clearer competitive procurement process which demonstrates equal access to State business for all vendors. The Division has been working with the Division of Procurement to improve its methods for purchasing client services. The Division will have its revised procedures in place by October 1, 1997, or as soon thereafter as approved by the Division of Purchasing.

Contract Management Needs Improvement

Contract monitoring has two objectives: (1) to ensure legal obligations are fulfilled by the contractors and (2) to ensure that acceptable levels of service are provided. In Fiscal Year 1996 the Division had contracts with eight vendors, and eight school districts who participated in the School to Work Alliance Program (SWAP). In addition, the Division had 11 inter-agency agreements with school districts to participate in the SWAP program, and also one intra-agency agreement with the Division of Developmental Disabilities Services, and one with Mental Health Services (which covers mental health centers throughout the State).

The Division uses two different methods to monitor its service provider contracts. Three of its contracts with outside vendors and its intra-agency agreements with the Division of Mental Health and Developmental Disabilities Services are monitored centrally by Division staff. For those contracts that the Division monitors centrally,

we found evidence of contract monitoring for both intra-agency agreements, but found evidence of contract monitoring for only two of the three contracts with outside vendors.

The remaining 13 contracts and 11 inter-agency agreements are supposed to be monitored by field office counselors. In fact, in a memo explaining the Division's contract monitoring procedures for those contracts that the Division does not monitor centrally, one staff person said, "there is no monitoring or administrative oversight conducted by the State Office. The State Office does not keep a list of who has been served through each contract nor do they maintain billing information."

According to the federal "Common Rule," "grantees and subgrantees will maintain a contract administration system which ensures that contractors perform in accordance with the terms, conditions, and specifications of their contracts."

Without adequate contract monitoring procedures, the following may result:

- The Division cannot ensure that all contract requirements were met by the service provider. For example, one contracted service provider was to provide marketing and employer development services. At the time of this audit, the Division had not yet checked to ensure that the contractor provided the required number of activities as stated in the contract. Division staff responsible for monitoring this contract did not check to determine whether this contractor complied with all contract requirements until March of 1997, seven months after the end of the contract period (September 1995 through August 1996).
- The Division cannot be sure that it did not pay more than the contract amount to the service provider. For example, in Fiscal Year 1996 the Division contracted with a service provider to provide \$108,000 in supported employment services. In addition to the \$108,000 in contract services, counselors authorized an additional \$222,000 in services for which no contract was used. Of this amount, nearly \$44,000 was for services which can sometimes be categorized as supported employment services. However, it is unclear from the Division's vendor expenditure report whether the \$44,000 in services was for additional supported employment services that should have been added to the original contract.
- The Division cannot determine whether the service provider is providing the quality and quantity of goods called for in the service contract. The State Contract Procedures Management manual states that "a signed contract does not relieve the State of the ultimate responsibility for the quantity and quality

of the goods and services provided. For this reason, an individual, or individuals, should be designated as contract manager(s).”

According to administrative staff, counselors will only authorize services to be provided by service providers who provide high quality services. While counselors agree that they do monitor the quality of services received by their clients through client feedback and client progress reports, they do not believe that it is their responsibility to ensure that certain service providers are complying with the terms and conditions of their contracts, or that the contractor is paid only the amount of its contract. In fact, few of the counselors are familiar with the contracts the Division may use to purchase services from service providers.

Recommendation No. 10:

The Division should:

- (a) Develop a contract administration system, as required by the Federal Common Rule, which includes clear policies and procedures for contract monitoring, including the definition of staff responsible and clearly defined objectives and monitoring activities.
- (b) Ensure that counselors’ practices comply with these policies and procedures in an ongoing way.
- (c) Monitor closely counselor performance in this area for at least the next six months.

Division of Vocational Rehabilitation Response:

Agree. The Division agrees that its contract management practices need review and adjustment on an ongoing basis. The Division intends to implement the following mid-course improvements to its contracts management by October 1, 1997: 1) clarify through policy counselors’ and supervisors’ roles in monitoring services and contracts; 2) train counselors and supervisors on their contract monitoring responsibilities; and 3) incorporate a centralized administrative contract management oversight function to assure counselor monitoring and accountability.

Department of Local Affairs

Introduction

The Department of Local Affairs is responsible for strengthening local government by encouraging local initiative and coordinating information and assistance to local governments. To accomplish its mission, the Department is involved in a variety of community development activities involving training, technical and financial assistance, and advocacy. The Department has eight divisions to carry out these services:

- Executive Director's Office
- Community Partnership Office
- Local Government
- Housing
- Field Services
- Property Taxation
- Economic Development
- Board of Assessment Appeals

The Community Partnership Office

The Community Partnership Office administers a state-funded grant program which provides funding for community-based youth crime prevention and intervention programs. The Youth Crime Prevention and Intervention (YCPI) Program was created in 1995 and received general funding of \$8 million in Fiscal Year 1998. The following comments and recommendation are from the Fiscal Year 1998 Youth Crime Prevention and Intervention Program performance audit.

The following comment and recommendation is from our August 1997 performance audit of the Youth Crime Prevention and Intervention Program at the Department of Local Affairs.

The YCPI Program Has No State Funding Available for Administrative Costs

Running the YCPI Program involves considerable effort on the part of the Department. Key activities conducted by Department staff include developing processes to allocate funding to nearly 200 grantees each year and then monitoring

the effectiveness of each program that receives funding. Since its creation in 1995, the Department has never received any state funding to administer the YCPI Program. All funds appropriated to the YCPI Program are intended to be allocated to communities in the form of grants or, more recently, set aside specifically for evaluation activities. As a result, Department staff charge the administrative expenses associated with YCPI (mostly personnel services) to federal programs they administer. These programs include the Americorps Community Service Program, the Safe and Drug-Free Schools and Communities Program, and the Community Service Block Grant Program.

On average about 18 individuals within the Department have worked at least part-time on the YCPI Program each year. Currently about 11 individuals spend some time working on YCPI-related functions. Given current staffing patterns, we estimate that it would cost at least \$266,000 each year (about 5.5 FTE, salary and benefits) to administer the YCPI Program. These costs are now absorbed as shown in the following table:

Youth Crime Prevention and Intervention Program Current Allocation of Personnel Services Costs	
Program	FTE Allocated to Program
Americorps Community Service Program	.35
Safe and Drug-Free Schools and Communities Program	2.66
Community Service Block Grant	1.91
Other (Governor's Office, Colorado State University, General Fund)	.58
TOTAL	5.50
Source: State Auditor's Office analysis.	

Operating costs for the YCPI Program are absorbed into the Community Partnership Office's general budget. Department staff estimate annual operating and travel costs for the YCPI Program to be approximately \$50,000.

Federal Guidelines Require Personnel Activity Reporting Systems To Reflect Actual Activity

The Office of Management and Budget's Circular A-87 states that, for the purpose of allocating costs to federal awards, "personnel activity reports...must reflect an

after-the-fact distribution of the actual activity of each employee.” The current method for tracking and reporting staff activity for the three federal grants administered by the Department does not reflect the actual activity of each employee. This is because the Community Partnership Office’s time sheets do not allow staff to charge activity to the YCPI Program, even though most of the staff perform work related to it. Thus, time that is spent on the YCPI Program is charged to one or more of the federal grants. We believe this practice is questionable because it results in an inaccurate distribution of personal services costs to these federal grants.

Department staff provided several explanations for the current cost allocation system. Staff reported that because the programs they fund through the YCPI Program are in the “same context” of the federal grant programs and because of the “open nature” of the federal programs, allocating YCPI costs to the grants is acceptable. Further, the Community Service Block Grant allows states to use up to 5 percent of their funding for “discretionary projects” and another 5 percent for administrative expenses.

We found it difficult to support the Department’s position that these programs operate in the same context. The three federal grant programs and the YCPI Program are similar in that they provide funding for communities to address various social problems. However, the programs do have somewhat different missions and grantees and, consequently, different monitoring and oversight requirements. Further, when we compared the grantee lists for the programs, we found that only 6.9 percent of the Fiscal Year 1997 YCPI grantees received funding from Americorps or Safe and Drug-Free Schools and Communities. We could not compare YCPI grantees with Community Service Block Grant recipients, because all Colorado counties receive these funds on a formula basis. Some YCPI grants are, however, allocated to county governments.

The Department Should Seek Other Funding Sources or Clarify its Authority to Use Federal Funds for Administrative Costs

Since continuing to use federal funds to administer this state program is questionable, the Department should pursue other sources of funds to pay the costs of administering the YCPI Program. One option is seeking authority to use a portion of the YCPI appropriation for administration. In the absence of state funding, the Department should determine whether it can secure appropriate federal funding to run this program or it should clarify its authority to use existing federal funding sources for this purpose.

Recommendation No. 11:

The Department of Local Affairs' Community Partnership Office should pursue appropriate funding sources for the administrative costs associated with the YCPI Program. This should include obtaining authority to use a portion of the YCPI appropriation or other sources of state funding sources for administrative costs and/or determining whether ongoing federal funding can be used for this purpose.

Department of Local Affairs Response:

Agree. Although the Department is confident that its funding partners have been advised of and are aware of its use of their funds to assist with the implementation of the YCPI Program, the Department will work with the appropriate funding agencies to address the concerns of the State Auditor's Office. The Department will seek written confirmation from the various agencies that they are aware of and accept the use of their funds for the purpose of supporting the YCPI Program through administrative, quality assurance, and technical assistance activities. Should any of the funding sources express concern over such use, the Department will adjust funding accordingly and will advise the appropriate legislative and executive budget agencies.

December 1997 Update:

Subsequent to the audit the Department reported the use of Community Services Block Grant funds for administrative costs associated with the YCPI Program to the Joint Budget Committee in a public hearing. A summary of these proceedings will be forwarded to the appropriate authorities at the U.S. Department of Health and Human Services for their review and approval. The use of staff paid through the Americorps Community Service Program to provide YCPI-related services has been discontinued. The Department is in the process of informing the appropriate federal agencies regarding the use of Safe and Drug Free Schools and Communities funds for costs associated with the YCPI Program.

Department of Natural Resources

Introduction

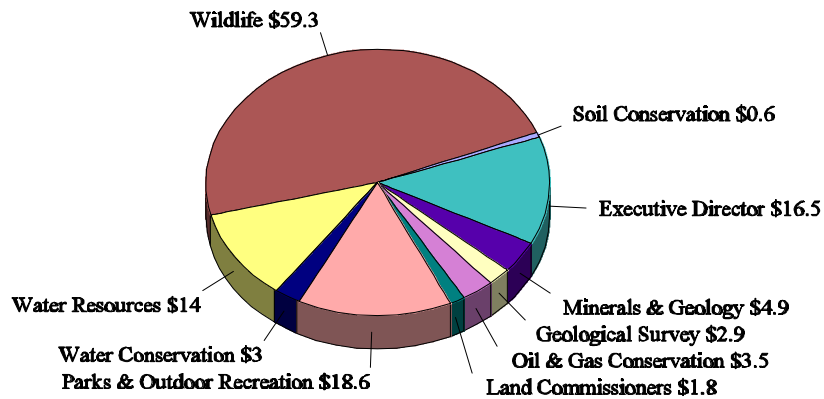
The Department of Natural Resources is responsible for encouraging the development of the State's natural resources. Resources include land, wildlife, outdoor recreation, water, energy, and minerals. The Department operates under the authority of Section 24-1-124, C.R.S., and is composed of an Executive Director's Office and the following nine divisions:

- Wildlife
- Water Resources
- State Board of Land Commissioners
- Soil Conservation Board
- Parks and Outdoor Recreation
- Oil and Gas Conservation Commission
- Minerals and Geology
- Colorado Water Conservation Board
- Colorado Geological Survey

The Department's Fiscal Year 1997 operating budget was about \$125 million with 1,422.4 FTE. The majority of the Department's funding comes from various cash funds, including hunting, fishing, and other licenses, royalties and rents, interest, and other sources. The following graph shows the breakdown of funds appropriated for the Fiscal Year 1997 operating budget by division, board, and commission.

Budget by Division/Board/Commission

(In Millions)



Source: State of Colorado Joint Budget Committee Fiscal Year 1997-98 Appropriations Report.

Improve Timeliness of Filing of Federal Financial Reports

The Department administers approximately 200 federal grants each year. Expenditures for these grants totaled more than \$15 million during the fiscal year ended June 30, 1997. Federal agencies require the submission of financial status reports quarterly, annually, or at other specified time intervals depending on the grant. Usually these reports are due 30 or 90 days after the end of the reporting period, as stipulated in the terms of the grant.

During our test of federal financial reports, we found that financial status reports for 5 of the 25 grants tested were filed after the due date specified in the grant agreement. Three of the past due reports were late by 22 days to 4 months. The other two were late in excess of one and three years, respectively. We noted a similar number of late submissions in the prior year. Lack of compliance with grant requirements could result in the delay or loss of future federal funds. Receipt of federal reimbursements

could also be delayed until the reports are filed, reducing the amount of state funds available for other projects or investment.

In response to this problem, the Department developed and is implementing a centralized report tracking database system for federal grants. This system generates a listing of reports due during a particular month to aid in the preparation and submission of financial reports in a timely manner. The system is operational and the new grant accountant has been reviewing all information entered onto the system for completeness and accuracy.

Recommendation No. 12:

The Department of Natural Resources should complete the review and correction of information on the report tracking system by December 31, 1998, to ensure that schedules generated by the system contain correct due dates.

Department of Natural Resources Response:

Agree. The new grant database continues to be developed and implemented during Fiscal Year 1998. This database provides for more accurate and timely monitoring of grant reporting and billing activities. However, several older grants which were awarded in prior years must still be individually researched in order to verify the exact status of the grant and make necessary corrections. As these older grants expire and are closed out, the time required to research problem areas will substantially decrease. All information on new grant awards is verified as it is entered in the database.

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Department of Public Health and Environment

Introduction

The Department of Public Health and Environment is authorized by Section 24-1-119(1), C.R.S. The Department is responsible for monitoring environmental quality, assuring the quality of health services, and maintaining health data for the State. The mission statement states that the Department is “dedicated to protecting and improving the health and environment of the people of Colorado.” The 11 major divisions are as follows:

- Health Facilities
- Emergency Medical Services and Prevention
- Disease Control and Environmental Epidemiology
- Family and Community Health Services
- Health Statistics and Vital Records
- Air Pollution Control
- Water Quality Control
- Hazardous Materials and Waste Management
- Consumer Protection
- Laboratory and Radiation Services
- Administrative Services

For Fiscal Year 1997 the Department had an operating budget totaling \$203,425,246. This budget supports 1,069.7 full-time equivalents (FTE).

The following comments and recommendations were prepared by the public accounting firm of Johnson, Holscher & Company, P.C., who performed audit work at the Department of Public Health and Environment.

Continue Efforts to Implement Indirect Cost Methodology

In Fiscal Year 1997 the Department received more than \$141 million in federal grants. The federal government reimburses the Department for those costs that are directly

related to the purposes of the grants, such as the compensation of employees who specifically performed work in the grants. In addition, the federal government allows the Department to recover a portion of the costs that indirectly benefit the grants such as the salaries of administrative personnel and office supplies. The Department has determined that many of the divisions' administrative costs indirectly benefit the federal grants. A new method for allocating these administrative costs has been implemented.

Prior to 1996 various methods were used to allocate divisions' administrative costs to federal grants. Beginning in 1996 a new methodology, a statistical distribution system, was used by three divisions within the Department. This system accumulates the administrative costs and proportionally spreads them to federal grants on the basis of the direct employee time charged to each grant. Although this methodology will not significantly change the total costs recovered, it is a more accurate and organized method to capture and allocate the costs. The use of this methodology by all divisions should provide consistency within the Department.

Although federal regulations allow the use of a statistical distribution system, the Department is required to obtain approval from the oversight federal agency, the U.S. Department of Health and Human Services. This approval has not yet been obtained. Without the proper approval, all costs charged to federal grants using the new method could be disallowed, requiring the Department to refund the costs.

Recommendation No. 13:

The Department of Public Health and Environment should continue to seek approval from the oversight federal agency for the statistical distribution system. In addition, the system should be implemented on a departmentwide basis.

Department of Public Health and Environment Response:

Agree. The Department has requested approval from the U.S. Department of Health and Human Services, our cognizant agency, for the statistical distribution system. Although Health and Human Services has not responded, we will continue to seek approval for the system.

In addition, the Department is currently evaluating the applicability of the statistical distribution for each division and section of the Department. We plan to implement the system in all areas where we believe it is appropriate.

Determine That Costs Are Funded From the Proper Revenue Source

The Emergency Management Program within the Department of Public Health and Environment is responsible for statewide emergency response activities. The Unit's total Fiscal Year 1997 budget of \$506,741 was funded entirely from two federal grants. The Rocky Flats Agreement In Principle (AIP) was the largest of these grants. The Rocky Flats AIP provides funding for the "...direction and support for state activities that enhance coordination and capability to respond to possible incidents involving the release of hazardous or radioactive materials with off-site impact from the Rocky Flats Site."

The Rocky Flats AIP grant does not allow charges for general statewide response activities. However, we could not determine if this grant was charged for this type of activity. Prior to Fiscal Year 1998 the Unit's employees did not track their time spent on the various functions they performed.

In Fiscal Year 1998, of the Unit's total budget of \$506,707, a general fund appropriation of \$71,000 was provided. The employees have been directed to track their time spent on each function.

If the Rocky Flats AIP grant is being charged with unallowable costs, the Department may be at risk of having to refund those costs.

Recommendation No. 14:

The Department of Public Health and Environment should charge costs to the Rocky Flats AIP grant that are identified specifically with the performance of that grant. Other costs should be funded from the appropriate sources. To determine the adequacy of current funding sources, the Unit's employees should use accurate time reporting by function.

Department of Public Health and Environment Response:

Agree. Beginning in Fiscal Year 1998 Emergency Management Program employees began tracking their time related to statewide emergency response activities separately from their time related to federal grants. These general

statewide emergency response activities will be monitored throughout the year, and if it appears that the general fund appropriation is not adequate to cover costs, additional general funding will be requested.

Department of Transportation

Introduction

The Colorado Department of Transportation is responsible for programs that impact all modes of transportation. Its operations are governed by the State Transportation Commission.

About one half of the Department's expenditures are related to construction funded by the Federal Highway Administration (FHWA) and state capital construction funds. Most of its other expenditures are funded by the Department's portion of the State Highway Users Tax Fund (i.e., the State Highway Fund) and various aviation-related taxes. The Department also receives monies from other federal agencies that it passes through to local governments and other entities for highway safety and transportation improvement programs.

The FHWA funds are used for research, planning, and construction of highways. The State Highway Fund pays for highway maintenance and operations and about 20 percent of any highway construction not covered by FHWA funds.

The following comments were prepared by the public accounting firm of Cottrell & Associates, P.C., who performed audit work for us at the Department of Transportation.

Place Greater Priority on Subrecipient Monitoring

Federal regulations require that primary recipients of federal funding who provide grant assistance to subrecipients monitor those subrecipients. The purpose of the monitoring is to determine whether the funds passed through to the subrecipients are being used in accordance with applicable laws and regulations.

The Department of Transportation has established procedures to document whether subrecipients are in compliance with federal laws and regulations. The procedures include reviewing audit reports submitted by the subrecipients to determine if there were any questioned costs or significant findings, and following up to ensure corrective actions are implemented. For most of the programs administered by the Department, the

monitoring procedures are being performed. However, we noted that the Transportation Development Section which is responsible for three different programs with subrecipient grants totaling approximately \$1,800,000 for calendar year 1996 and approximately \$1,700,000 for calendar year 1995 did not perform a review of the audit reports received from subrecipients during Fiscal Years 1997 or 1996 in a timely manner. As a result, the monitoring requirement of the federal program is not being carried out, the grants to subrecipients may not be spent on approved programs, and the State could lose federal funding.

Recommendation No. 15:

The Transportation Development Section of the Department of Transportation should place a greater priority on reviewing subrecipients' audit reports in a timely manner.

Department of Transportation Response:

Agree. Procedures for subrecipient monitoring will be established.
